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75 Years Ago, a Great Canadian Solved the Problems Engulfing the World Today

A Vancouver high-school drop-out, G.G. McGeer, beat John Maynard Keynes by several years in figuring out the mysteries of money and the wiles of unrestricted banking years. And, there was no let-up in his wit in tracking down the surrender of reformers, who had traded conformity for a title or a cushy appointment. Eventually he earned a law degree, became mayor of Vancouver and ended up as a Canadian senator. For years he served as the bumble-bee on Prime Minister Mackenzie King's bottom that left him with little choice but to nationalize the Bank of Canada. It had been founded as a private institution only four years earlier by a Conservative government.

Nor did he stop there: he went on to analyze the betrayals of monetary reformers bribed and fawned upon into passive conformity. And delving into the origins of banks, he tracked the processes by which from providing useful services, they have come to undermine society and hasten its ultimate collapse. And from all this he reflected with great originality and depth about the essence of money.

As representative of the Vancouver, New Westminster Trades and Labour Council, he reported: "In pursuance of the instructions contained in your letter of 10th August, I appeared before the Royal Commission in Banking, Currency and Economy at its sittings in the Court House in this City on the 16th ult.

"In the short time at my disposal it was not possible to present a closely reasoned brief upon the many phases of the monetary and economic situation with which organized labour is definitely concerned.

"In addressing a properly constituted, impartial tribunal charged with the great responsibilities that this Commission has undertaken, all will agree that both fact and argument should be presented in restrained language, advancing plain reason and simple logic. There is, however a proper time and place in advocacy for appeal, conciliation, argument and denunciation. Upon this occasion I determined that the course most likely to produce results beneficial to labour called for 'an evangelical bombardment of invective' directed at the private money system and proprietary interest….

"The Commission consists of:

"The Right Honourable Lord Macmillan, PC, KC, a man who has risen from the humble position of a Scottish minister's son, and who is now steeped in the tradition of institutionality that has generously bestowed upon him some of the highest honours in the gift of an aristocracy based on money power.

"The Honourable J.E. Brownlee, KC, lawyer premier of the Alberta farmer government. Sir Charles Addis, KCMG, a director of the Bank of England, an institution whose monetary policy has brought Great Britain and every other nation, including Canada, which has attempted to follow it, into a veritable chaos of unemployment and bankruptcy.

"Sir Thomas White, PC, KCMG, Vice-President of the Canadian Bank of Commerce, and Canadian war-time Minister of Finance, under whose ministry war-time rates of interest charged to government for credit loans were increased by 50%, while, as an added inducement to credit dealers to plunder a nation at war, Victory Bonds carrying 5.5% were issued free from taxation. He was Minister in 1914 when

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Great Canadian *from page 1*

$10,000,000 of Dominion legal tender currency notes were issued unsecured by gold and paid out on account of the Canadian Northern Railway, the bankrupt undertaking of MacKenzie & Mann.

"Beaudry Leman, BSc, CE, General Manager La Banque Canadienne Nationale, was formerly President of the Canadian Bankers' Association. Mr. Leman is reported, in an extract from *The Organizer,* Vol. XII, No. 3, page 39, as stating on November 16th last to a meeting of the Purchasing Agents' Association:

"A symptom of that disorderly metabolism may be found in the attempt to maintain high wage rates and reduce the number of working hours. I suggest reverting to a twelve or fourteen-hour day of labour.

"Now while it is quite true that on the following day this bald statement was denied and qualified, the correction clearly indicated Mr. Leman's adherence to the outworn theory of banker management under which bankers, by lowering interest rates and encouraging borrowers to accept credit loans repayable in money, create booms of prosperity. And then, by raising interest rates and withdrawing and withholding credit loans from circulation, precipitate depression crises.

"This theory compendiously described as 'bank rate policy' permits the banker to profit by loaning the people credit when they do not need it and take their securities away from them by demanding repayment in money which borrowers cannot secure for the simple reason that it does not exist.

"In describing the effect of this policy on business and wage-earners, the Macmillan Commission report says: 'Its efficacy depends upon reducing business profits and increasing unemployment up to what figure is necessary to cause business men rather to decrease their cost by additional economies or to insist on and their workers to accept a reduction in wages.' (Section 221).

"In view of the fact that our railways, the largest employers of Canadian labor, are at the present time demanding that a substantial section of their employees accept a further cut of 10% in their wages, and at the same time the government is encouraging the raising in the level of prices of necessities, the attitude of the members of the Commission to banks rate policy is of public interest.

"Lord Macmillan's attitude may, I think, be properly inferred from the language used in describing a theory of trade management employed by bankers which involves the reduction of business profits, the increase in the hours of labour, the reduction of wages and the increase in unemployment, which is contained in Section 218 of the report of which he is the author. It reads:

"Bank rate policy…is a most delicate and beautiful instrument for the purpose.

"I am afraid that wage-earners from whose ranks the army of the unemployed has been developed, will find difficulty in agreeing with this conclusion.

"Labour, industry, commerce, and academic economy are not represented on the Commission. It is a bankers' enquiry. The destiny of the nation, the well-being of the people and the general standard of living are placed within the power and under the control of men engaged in a business that prevents them from acting with freedom in the public service. The plain fact is that the government has entrusted the standard of living of the people to the care of the very men that the government should have guarded the people against.

"No provision has been made to provide the people with Counsel for the purpose of protecting the interests of the public.

"In view of the power to establish facts and to propose changes in our Canadian banking and currency laws, now vested in Lord Macmillan, I think there are certain matters relating to his public service in Great Britain with which you should be acquainted.

"As the Right Honourable H.P. Macmillan, KC, he was Chairman of a Royal Commission appointed on the 5th day of November, 1929, by the British government 'to enquire into banking, finance and credit, paying regard to the factors, both internal and external, which govern their operation, and to make representations calculated to enable these agencies to promote the development of trade and commerce and the employment of labour.'

"The Committee, consisting of bankers, business men, industrialists, economists and representatives of labour, filed their report on June 23, 1931. For his service the Chairman was apparently promoted to the Peerage along with Philip Snowden, who was responsible for his appointment and who is now the most outspoken champion of the Bank of England, Montague Norman and the gold standard.

"In a reservation to the report filed by Sir Thomas Allen and Mr. Ernest Bevin, the following disconcerting statement is made: 'We also desire to point out that the Committee decided to examine monetary policy only on the basis of the gold standard and, therefore, no alternative was examined or discussed.'

"The decision of the majority members of the Committee, unsound in law, satisfied the desire of and served effectively the private money system which secures its power and profit from the shortage of money that the gold standard deception maintains. No matter what the national situation was, there was no good reason why an alternative basis should not have been considered.

"Within three months of the filing of the report, the policy of the Bank of England, which Lord Macmillan and a majority of the Committee endorsed, had reduced Britain to a state of bankruptcy. England was forced to abandon payment in gold, but she has not yet repudiated the private management of public credit, nor has she abandoned the gold standard insofar as it denies to government the right to issue national currency and public credit free of interest charge, and compels the government to pay an unnecessary toll of interest to bankers for the public credit now used to finance public enterprise."

A Needless Toll of Interest

"That is the outstanding feature of the gold standard money system from a banker's point of view, and the part to which the public, unfortunately, gives the least attention.

"Canada, Great Britain and the US still maintain this feature of the gold standard. Certainly the Bank of England in 1931 has not changed the attitude with which it dominated the Macmillan Committee in 1931. It was openly associated with the gold standard group which wrecked the economic conference recently abandoned in London.

"There is no good reason for believing that Lord Macmillan in Canada in 1933 will repudiate Lord Macmillan in England in 1931 by disagreeing with his colleague Sir Charles Addis who as a Director of the Bank of England, is now one of the official priests in the 'High Cathedral of Usury.'

"It is difficult to believe that Lord MacMillan and Sir Charles Addis were selected by the Right Honourable Mr. Bennett for any other reason than that their views on fiscal policy coincide with those of Mr. Bennett, who is reported to have publicly stated as recently as September 1st the following:

"The monetary committee of the World Economic Conference accomplished a tremendous amount of good. It reaffirmed gold as the only satisfactory medium of exchange. It was also agreed that paper money must have a backing of metal reserves…. Canada's national life depends on the maintenance of her position as a great exporting nation and therefore this country cannot experiment with shorter hours of work and higher rates of pay.'

"Apparently Mr. Bennett, at the time of Lord Macmillan's selection, had fallen completely under the spell of the men in London who were conspiring to enslave mankind with a gold standard money system. He is willing to permit international credit dealers to do to the Canadian wage earner and wealth producer what President Roosevelt definitely refused to permit them to do to the wage earners and wealth producers in the US.

"Under such circumstances the appointment of Lord Macmillan, Sir Charles Addis, Sir Thomas White and Mr. Leman to investigate the Canadian monetary system should be viewed by all wage earners, business men and wealth producers with fear and grave misgiving.

"[Given] the charge made by men in every walk of life that the existing economic disaster is due in substantial measure to the mismanagement of the banking system by banking authorities, this Commission, consisting of bankers and a safe chairman from the bankers' point of view, offers a unique example of a group of men conducting an investigation of matters wherein the conduct of some of the Commission members should properly be the subject of the enquiry. If the charge were made that this Commission might be likened to a 'thieves' kitchen court, in which the wrong-doers were both upon the Bench and in the Jury box,' I do not see how it could be successfully refuted.

"This Commission stands condemned under 'the ancient truth' that propounds this postulate:

"When the lucrative profession of usury becomes likewise a post of honour, the State is ruined and the people are doomed to the wretchedness of destitution.

"I cannot see how bankers can investigate their own mismanagement.

"Nor can I see how this Commission can investigate the management of national currency and public credit during the time that Sir Thomas White (formerly connected with the financial groups closely associated with MacKenzie & Mann and the Canadian Bank of Commerce) was Minister of Finance.

"It is impossible to believe that Sir Thomas White and Mr. Leman can, with any degree of comfortable safety, conduct an enquiry into the credit peregrinations of Sir Herbert Holt as President of the Royal Bank of Canada; nor are they likely to disclose the more than significant relations that exist between finance and industry when so prominent an industrialist as Sir Charles Gordon presides over the destinies of the textile industry and the Bank of Montreal.

"There is not the least prospect of this Commission investigating and disclosing the truth in detail of the transaction last November wherein the government advanced to the banks $35,000,000 in Dominion legal tender notes by making a double shuffle of Dominion 4% notes, bank credit and legal tender currency notes. At the time the issue was made the Prime Minister declared that:

"It was in accordance with the idea that the easing of money is highly desirable in the interest of business recovery,' indicating that credit was tight and would be loosened up.

"The confusion that was engendered when Mr. M.W. Wilson, as Manager of the Royal Bank at its last annual meeting declared:

"At no time during the present depression has it been necessary to withhold bank credit for commercial purposes when proper security was offered will no doubt remain undisturbed.

"The attitude of this Commission in Canada to the great problem of public management of public credit will be identical with the attitude taken by Lord Macmillan and the majority of the members of his Commission in 1931. It will not even be considered.

"It would be a great mistake to permit the public to believe that Lord Macmillan is either representative of the progressive thought of Commercial Great Britain or that he was in any way a contributor to those sections of the Macmillan Commission that are now worthy of consideration.

"In less than two short years passing events have proven the main reports, the only part with which Lord Macmillan was associated, to be unsound, impracticable, wholly in error in its interpretation of established fact, and wrong in every detail where the anticipation of future possibilities was assumed.

"That commercial Great Britain is no longer willing to accept blindly the blind and misguided leadership of the Bank of England and the author of the Macmillan report is now definitely indicated. As recently as July 29 of the present year I received a letter from the Secretary of the Empire's most representative commercial and industrial organization, the London Chamber of

Commerce, in which he said:

"I think we all owe a very great debt to the American President for having defeated the conspiracy at the Economic Conference to get the world back on to gold. I agree with you, however, that unless he appropriates the national credit to give the people of the States the necessary purchasing power to enjoy the vast abundance of real wealth which is at their disposition, his domestic policy must in the long run fail."

"In the July 1933 issue of its official publication, that great organization of Great Britain's industrial leaders repudiates the policy of the Bank of England and the recorded views of Lord Macmillan and Mr. Bennett in these unmistakable statements:

"Having evaded recognition of the root cause of the trouble, which, as has been consistently stated by the London Chamber of Commerce for the last eighteen months, is a vicious monetary system, the Conference will now concentrate upon trying to mitigate its effects. The problems of tariffs, exchange restrictions and quotas, cannot be solved until the monetary system has been reformed, nor can prices be raised and stabilized. There is about as much chance, with the restoration of the old monetary system in sight of inducing nations to modify their tariffs or exchange restrictions, as there would be persuading by argument a drowning man to leave go of a life-buoy. He must first be lifted out of the water, life-buoy all and then, finding himself safely seated in a boat, he will begin to wonder that he has the lifebuoy around him, wriggle out of it, and cast it into the water.

"That the conventions of the International Gold Standard are so fundamentally opposed to modern social and economic conditions that no government could, even if it wished to, give effect to them. The International Gold Standard system is an anachronism in the Twentieth Century. It can never again function, but as its high priests still hold sway over the nations and regard it sacrilegious even to discuss alternative systems, there appears to be nothing for it but to await the further inevitable collapse of the structure built upon it."

In the face of this conclusion expressing the opinion of unbiased and unquestionable authority, the appointment of Lord Macmillan, a Director of three Bank of England and two Canadian bankers to find Canada's way out of the Depression might well bring people to a realization of our ex-Prime Minister Mr. Bennett's conclusion: "Nothing but the Grace of God can save us in this crisis."

We are back there once more with the stakes even more steeply favoring speculative cowering behind an ever higher technology of swindle and ever more murderous military might.

And our promising reformers today even without the prospects of lordships are woefully short of the high spunk and genius for analysis that animated McGeer.

That shines through in McGeer's appearance before the Commission in Vancouver to present the Macmillan Committee Minority Report.

I quote: "The Macmillan Committee's report will be recognized by historians as an epochal monument in the record that mark the ordered progress of the evolution of enlightenment.

"I believe this to be true because the members of the Committee were skillful enough and sufficiently wise to write in to the main report qualifications and findings of fact and to lay down specific recommendations, from which can be drawn a plan of fiscal and economic reconstruction and policy that will satisfy the needs of twentieth century progress. Everything and more than Roosevelt's 'Brain Trust' has yet attempted was considered and proposed.

"With this Lord Macmillan is in no way associated. It contains a definite scheme of national management of public credit, the deliberate regulation of domestic and international trade and the use of public credit as the means of financing public enterprise, social services and the improvement of the general standard of living."

National Banking

"My conclusion in this regard is based upon the following extracts which I believe contains a definite scheme of national management of public credit, the deliberate regulation of domestic and international trade and the use of public credit as the means of financing public enterprise, social service conclusion that the minority, consisting of J. Maynard Keynes, Reginald McKenna, Sir Thomas Allen, Ernest Bevin, J. Prater Taylor, A.G. Tullock, and Sir Walter Raine, would now agree upon and present as the minority findings, if the report were being written today.

(1) 'The Bank of England ought to be transformed into a public corporation" (page 240).

(2) "The monetary system must be a managed system, operated by individuals placed in a position of unchallengeable independence" (Section 280)."

The acceptance of these conclusions would completely destroy the bankers' monopoly of public credit management for private gain. Public service and private profit do not go together.

Public Credit

(3) "The vicious circle is now complete. The decline of new enterprise has reacted adversely on profits and prices, and the low level of prices stands in the way of new enterprise. It is for this reason that some of us think that in the domestic field it may be necessary to invoke government enterprise to break the vicious circle" (Section 316).

(4) "The best hope of a remedy lies in a monetary policy designed to increase the volume of purchasing power" (page 190).

(5) "It is not necessary that the volume of note issue (*a fortiori,* or the creation of national bank credit) should continue to be regulated as it is now by reference to the amount of gold held in reserve" (Section 148).

(6) "Since the bankers as a whole under banking practice maintain a cash proportion of deposits of roughly 10% of the cash held in reserve (i.e., legal tender paper money borrowed from the Bank of England or the Department of Finance in Canada) the bulk of the bank deposits arise out of the actions of the banks themselves, for by granting loans, allowing overdrafts and purchasing securities, a bank creates a credit in its books which is treated as the equivalent of a deposit of money" (Sections 71 to 74 inclusive).

(7) "The theory that governmental expenditure in the promotion of public enterprise and social service is restricted by the accumulated savings available for investment is erroneous. When governments distribute wages by financing public enterprise with national currency and credit, the volume of capital investment is increased") (Section 47 of Addendum 1, page 203 and Section 24 of main report).

(8) "If governments pursue an inflationary policy, i.e., meet expenditures not out of revenue, but by the issue of paper currency for the creation of credit in a national banking system), forces are set in motion increasing profits and wages and additional spending arises" (Section 24).

During the war period the bank deposits in Great Britain rose from less than £1,000.000.000 to more than £2,000,000,000. In the US. They were increased from $18,000,000,000 to

$37,000,000,000, and in Canada the increase was from less than $1,000,000,000 to $2,400,000,000. Our prosperity continued until this enormous increase in purchasing power was withdrawn from circulation by interest and profits allocated to capital. The fact that the total accumulation of money wealth alleged to be on deposit in the banks in 1914 was increased by more than 100 per cent during the period of war when wealth in the form of life and property was being destroyed proves that the creation of purchasing power upon which progress depends is an independent economic function of the government. The fact that the credits were created in private banks does not affect the conclusion in any way because the banks themselves are the creatures of the government, taking their right to operate from the charters issued under the banking laws. They are merely exercising a delegated authority of government.

By nationalizing the management of the issue and circulation of national currency and public credit, the government becomes possessed of the economic organization from which may be secured an inexhaustible supply of governmental purchasing power. This purchasing power can be used to finance progress and eliminate unemployment, by advancing the intellectual and cultural tone of public opinion and the health and contentment of the people.

Governments, by paying national spending power out for public enterprise and social service that improve the outlook and contentment of the people as a whole, are investing public credit in the best reserve that can be developed for maintaining the stability of government and the economic stability of the social system. It is in this power of government to issue its own purchasing power that we find the way to extend to mankind the enjoyment of the standard of living that an age of plenty warrants.

The adoption of these conclusions of the minority members of the Macmillan Committee would deny to the banker the right to create purchasing power in the banker's books by the mere stroke of a pen but it would open the way to the conquest of poverty.

Surely, what the banker has been able to do with the manipulation of credit for the banker and financier can be done for the benefit of the people and the State.

The lucrative business of converting public credit into private bank credit and loaning it at interest to the government at the expense of the tax-payer as a private banker's monopoly would be eliminated and the use of public credit as the means of financing twentieth century progress would be restored to responsible government. Taxes other than regulatory would, like the gold standard would become relics of the illiterate past.

Public credit would become the "economic blood-stream" of the social system, and the going concerned activity of human progress would take the place of gold as the security for the value of all wealth, real and representative, including gold, silver, paper currency and credit in the banking institutions.

By these findings of fact, the members of the Committee responsible for them have shown the way by which the purely artificial shortage of buying power can be overcome simply by eliminating the impossible money and credit cost that the private money system imposes upon the circulation of credit as the purchasing power of government and commerce. They point to the way that will serve our greatest necessity, that of financing both government and progress.

By changing the administration of public credit from a private profit-making privilege to a public trust, the spending power of government can be increased and the buying power of the consumer can be sustained.

Price Control and Trade Management

(9) "Gold reserves are held today solely to meet temporary deficiencies in the balance of international payments" (Section 340).

(10) "The circulating media consists overwhelmingly of paper money and bank deposits. It is this volume of purchasing power which directly affects the price level and not the amount of gold which may be held in reserve" (Section 45).

(11) "There is nothing inherently impractical in the exercise of the government's power to deliberately control the price level. We should be ready to attempt the task and to gain experience by practice) (Section 210).

(12) "International trade can and should be regulated and controlled by deliberate management" (Section 41, Addendum 1, page 201).

"Here (we) find the sacred power of gold repudiated and a common-sense recognition of the necessity of setting up a system of regulated trade and planned economy under which the people can maintain a system of properly balanced government.

"The minority members of the Committee, in addition to these specific qualifications and conclusions, fully discussed the possibility of eliminating unemployment in Great Britain by State-aided industrial activity; the promotion of public enterprises such as electrification of the entire railway system; the reclamation of land by drainage; and the rebuilding of the slum areas of cities. The proposals were directed to breaking the depression by finding the means of distributing wages.

"Recognizing that there could be no substitute for the weekly pay check that provides the necessities and meager comforts of the worker's humble home, they tried to get Lord Macmillan and his associates to recommend a program more far-reaching than that which Roosevelt has inaugurated. They were unsuccessful in this attempt. They failed in their attempt to establish that the maintenance of the right of men and women to living wages is a more sacred responsibility of government than is the right of the usurer to the collection of interest, now nothing but the wages of book-keeping entries, because of banker opposition.

"The distinguished economists, J. Maynard Keynes, the minority leader on the Committee, recently summarized the attitude of the minority by saying:

"Let us rebuild our market within the area we control and by State action enforce a decent level of wage standards. To do this we must reorganize the entire economy, develop our resources to the full and maintain armed forces, not for conquest but only for the adequate defense of a peaceful Commonwealth."

William Krehm

As in Biology, a Tiny Negative Input can Have a Disastrous Effect

Is the parallel accidental or tell us about the human trait of transferring the patterns of technology to seemingly unrelated social areas?

The Wall Street Journal (3/05, "How a Little Subprime Lending Had a Big Impact" by Carrick Mollenkamp and Serena NG) informs us: "Even at its peak, subprime lending accounted for a relatively small portion of overall mortgage lending. Yet losses from these mortgages caused deep damage to the financial system.

"Now, documents released by Senate investigators last week provide clues to understanding why the losses were so severe. The documents show how Wall Street banks packaged and repackaged the same risky bonds into securities that ultimately helped magnify the impact of defaulting subprime mortgages on the financial system."

CDOs Infect Real Estate Like Deadly Germs

"In one case, a $38 million subprime mortgage bond created in June 2006 ended up in more than 30 debt pools and ultimately caused roughly $280 million in losses to investors by the time the bond defaulted in 2008, according to data reviewed by *The Wall Street Journal*.

"That was a central finding of the Senate investigative panel probing Goldman Sachs Group Inc.'s actions in the mortgage market. In a memo last week, Panel Chairman Sen. Carl Levin (D, Mich.) said Goldman's work 'magnified the impact of toxic mortgages' by replicating mortgage securities in debt pools known as collateralized debt obligations as well as CDO derivatives, and also in an index that tracks subprime bonds.

"The subprime mortgages that caused big losses generally were packaged into CDOs, in which dozens of mortgage-backed bonds were pooled together and slices of the CDOs were sold to investors. Another version of these CDOs didn't contain actual mortgage bonds but were linked to them via derivatives called credit-default swaps. Through the use of derivatives, banks created many of these synthetic CDOs using the same mortgage securities, all of which would rise or fall in value depending on how the mortgages were performing. With synthetic CDOs, those who had bet that the loans would perform well were on the hook if their performance deteriorated."

In mathematics, the expression "derivative" refers to the rate of growth, and the rate of growth of the rate of growth, to infinite degree. It is in effect the mathematics of the atomic bomb. The number of its terms can encircle the world and keep going. Its use, turning up in human affairs, cannot be of anything but ill omen.

Not surprising then that the *WSJ* should continue: "In effect, the document said Wall Street was 'copying and pasting' what turned out to be the worst-performing securities of the mortgage boom. Such activity helped multiply opportunities for hedge funds and traders who wanted to short the housing market, but magnified the losses of those on the other side of the trades. To short, in this instance, is to bet the housing market will turn down." ("To short" is to borrow something in order to sell it.)

"'There was a limited number of similar bonds,' said Darrell Duffie, a finance professor and derivatives authority at Stanford University. 'So they are likely to show up in multiple deals.'

"A Goldman spokesman declined to comment.

"An important moment in the housing cycle came in January 2006, a year before the downturn of the housing market had crystallized. That month, a consortium of banks, including Goldman and Deutsche Bank AG, with the help of a London data firm, launched an index, known as ABX.HE, which served as a proxy for subprime loans.

"For the first time, banks and hedge funds had an indicator of the prices of subprime-mortgage securities, and a somewhat active market to buy and sell credit protection against housing-market losses. The ABX.HE, one of four ABX indexes, was backed by 20 subprime bonds, some of which reappeared in numerous CDOs.

"By late 2006, Goldman had a large bullish position on the ABX, because it had taken the other side of bearish bets by hedge-fund clients, according to the Senate documents Subsequent deals would help reverse that position.

"One mortgage bond, Sound-view Home Loan Trust 2006-OPT5 M8, which eventually was a component of the ABX plus more than 30 CDOs, caused $280 million in losses.

"The Soundview deal in June 2006 bundled together roughly $3.1 billion in subprime home loans made by Option One Mortgage Corp. to 15,746 individuals across the country, with a high concentration in California and Florida, two states that were among the worst hit by the housing downturn. The securities from the deal were sold in slices with different credit ratings, interest rates and risk levels.

"One slice of the Soundview bonds, called MS, began making its way through Wall Street.

"About $35 million on the MS bond was issued, and it stood to lose money if roughly 5% of the loans in the pool were wiped out by losses.

"In July 2006, the Soundview deal was picked by Wall Street banks to be one component of the ABX, and the Soundview M8 bond was replicated in multiple CDOs. They included Goldman's Hudson Mezzanine Funding 2006 CDO, which took on a $15 million exposure to the Soundview M8 bond in late 2006, according to documents released last week by the Senate panel.

"Hudson represented Goldman's bearish view on housing. According to the Senate Inquiry, Goldman used the CDO to protect itself against losses by the $2 billion of assets referenced in the pool. Among the assets was $1.2 billion in bullish bets on bonds underpinning the ABX indexes. Goldman was buyer of protection from Hudson, meaning the bank had a bearish position on the same bonds.

"The Soundview MB bond appeared again in a CDO called Abacus 2007-AC1, the mortgage deal at the center of the Securities and Exchange Commission's civil-fraud lawsuit against Goldman. That CDO, which closed in April 2007, had a $22.2 million bullish position on the Soundview bond. Goldman has denied any wrongdoing in the case.

"Some Goldman employees appeared to be aware that the Soundview M8 bond was shaky by early 2007. In an April 2007 email, a Goldman trader included it in a list of what he called 'dirty '06 originations,' referring to the period in which lending standards loosed. By that time, about 8% of the loans in the Soundview pool already at least 60 days past due.

"In July 2007, Mizuho International PLC, a unit of Japan's Mizuho Financial Group Inc., seeking to break into the CDO business included the Soundview bond in a CDO 2007-1. That CDO had a $13 million exposure to the Soundview M8 bond, according to documents reviewed by the *WSJ*.

"In all, more than $280 million of bullish positions on the Soundview M8 bond were in at least 30 CDOs underwritten by various banks, according to data reviewed by the Journal. As defaults among the subprime loans backing the deals mounted in 2007, the M8 bond's value fell. The entire $38 million face amount eventually was wiped out.

"Anthony Sanders, a real-estate finance professor and authority on securitization at George Mason University in Fairfax, VA, said the problem was that the same mortgage bonds ended up in many deals, potentially multiplying the losses.

"'Serious problems with common [asset-backed securities] can decimate all CDO deals,' Mr. Sanders said."

The Perils of Depending on Technology

I have long felt that man has his horizons shaped by the patterns established in the fields of tech research. We live in an age when we communicate on the most intimate and vital matters with the rest of the world via tenuous information retrieved by a complex and ever-changing contact driven by ever-more-tightly controlled marketing.

There is, thus, little space left for reasserting where our society's interests lie. For that we require a heroic amount of catch-up in retrieving a knowledge of our history, and the powerful weapons of science. These, systematically expunged from our economic courses, to the belying of the very name "university," must be restored. Failing that, the mounting financial gambles swelled into exponential growth, can lead only to the ultimate and inevitably fatal of such gambles, atomic war.

William Krehm

Joining the Dots and Booby Traps Together

The Globe and Mail (15/05, "In Brief") has tapped a variety of divergent sources that prove the utter incoherence that marks the many places where logic and coordination is a key need that the political leadership of the world has completely lost sight of. The total effect is of being locked in a capsule heading for outer space, operated by experts who have lost the ability of keeping track of their laundry bill, let alone of their laundry.

We quote from their quotations:

From *The Associated Press:* "Space shuttle Atlantis thundered away on its last trip into orbit on Friday, hoisting an experienced crew of six and a full shipment of space station gear…. The biggest launch-day crowd in years packed the Kennedy Space Center….

"The shuttle's destination is the International Space Station, which was soaring over the South Pacific at the time of lift-off. The shuttle should catch up with the orbiting complex and its six residents on Sunday morning.

"This 12-day mission is the last one planned for the Atlantis, the fourth in NASA's line of space shuttles. Only two flights remain after this one, by Discovery and Endeavour. NASA plans to end the 30-year program by the end of this year.

"President Barack Obama wants NASA to focus on getting astronauts to an asteroid by 2025 and into orbit around Mars by 2035. He cancelled the previous administration's plan to return to the moon."

Again from *The Associated Press*: "Sacramento, Calif. – Governor Arnold Schwarzenegger on Friday called for eliminating California's welfare-to-work program, one of the deep cuts he proposed to close a $19 billion (US) budget deficit in the coming fiscal year.

"The Republican governor laid out the most severe cuts to health and welfare programs since the state tumbled into recession nearly three years ago. The Republican governor announced his revised budget plan for the fiscal year that begins in July, as the state's 12.6% unemployment rate ranks among the highest in the nation and tax revenue remains low.

""Schwarzenegger acknowledged the cuts will be painful, but said he has no other options because tax revenue has plummeted."

Tax revenue has plummeted because the same Obama government planning to send men to Mars couldn't bring itself to send for historians, economists fired from universities for teaching what the great economists learned about getting out of the Depression of the 1930s. Accept as government counselors former high officials of our deregulated gambling mega-banks and you have a perfect formula for losing the astronauts you are planning to send to Mars, for having skimped on the research costs of perfecting means of bringing them back to earth.

A further note: the crippling habits that we impose on governments' thinking – mistaking investment for social survival as extravagance that we cannot afford – is not confined to government financing. It cripples the performance of official and human thinking in other fields. That is an essential part of the inheritance that our economic teaching – especially in the 19th and 20th centuries had learned from the Aristotle and other Greek philosophers of the Socratic school.

Of this, *The Globe and Mail* provides us with a shocking example ("Famed Spanish Judge Faces Trial of His Own"): "The Spanish judge who became an international hero by going after Augusto Pinochet and Osama bin Laden was suspended Friday for allegedly abusing his authority by investigating atrocities committed during and after Spain's own ruinous civil war.

"Garzon, 54, has been removed from his post pending his trial on charges of knowingly going beyond the limits of his jurisdiction in 2008 by investigating the execution or disappearance of more than 100,000 civilians at the hands of supporters of General Francisco Franco during and after the ruinous Civil War.

"The punishment could effectively end Judge Baltazar's career."

Irrational mind-bending makes an investigation of oppression in far-off Chile tolerable, but bring the process home to Spain and it supposedly becomes unacceptable. You cannot use our minds and basic morality that way without bringing on disorientation in other fields.

W.K.

(SEE PAGE 2)

Washington Catches Up with Antics of Its Key Free-swinging Bank

A bit late in the costly game, but better late than never, the Securities Exchange Commission has charged with fraud Goldman Sachs, the mightiest of US banks, that practically designed the financial meltdown to maximize its profits.

The news came to us from an Associated Press dispatch carried by *The Toronto Star* (17/4, "Goldman Sachs facing fraud charges" by Marcy Gordon): "Washington – The US government has accused Goldman Sachs & Co. of defrauding investors by failing to disclose conflicts of interest in subprime investments it sold as the housing market was collapsing.

"The Securities and Exchange Commission said in a civil complaint Friday that Goldman failed to disclose that one of its clients helped create – and then bet against – subprime mortgage securities that Goldman sold to other investors.

"'Two European banks that bought the mortgage securities then lost nearly $1 billion (US),' the SEC said. The agency is seeking to recoup profits reaped on the deal.

"Goldman Sachs denied the allegations. In a statement, it called the SEC's allegations 'completely unfounded in law and fact' and said it will contest them.

"The civil complaint comes as legislators seek to crack down on Wall Street practices that helped cause the financial crisis.

"Among proposals Congress is weighing are tougher rules for complex investments like those involved in the alleged Goldman fraud.

"The Goldman client implicated in the fraud is one of the world's hedge funds, Paulson & Co.

"The SEC said it paid Goldman $15 million in 2007 to put together an investment offering…tied to some mortgage-related securities the hedge fund viewed as likely to decline in value.

"Separately, Paulson took out a form of insurance that allowed it to make a huge profit when those securities became nearly worthless.

"Goldman Sachs shares plummeted after the SEC announcement and closed down $23.57 (US) or just under 13% at $160.70 in a fall-off that also caused shares of other companies to sink. The Dow Jones industrial average finished $125.91 points lower at 11,108.66. The Toronto stock market was also down sharply, off 140.86 points at 12,070.66.

"The civil lawsuit filed by the SEC in Manhattan was the US government's most significant legal action related to the mortgage meltdown that ignited the financial crisis and helped plunge the US and much of the rest of the world into recession. The SEC's enforcement chief said the agency is investigating a broad range of practices related to the crisis.

"The agency also charged a Goldman vice-president, Fabrice Tourre, 31, who it said, was mainly responsible for devising the deal and marketing the securities. The SEC said he is now executive director of Goldman Sachs International in London. Tourre, the SEC said, boasted to a friend that he was able to put such deals together, as the mortgage was unraveling in early 2007.

"In an email to a friend, he described himself as 'the fabulous Fabstanding in the middle of all these complex, highly leveraged, exotic trades he created without necessarily understanding all of the implications of those monstrosities!!!"

"The SEC is seeking unspecified fines and restitution from Goldman Sachs and Tourre.

"Asked why the SEC did not also pursue a case against Paulson, enforcement director Robert Khuzami said: 'It was Goldman that made the representations to investors. Paulson did not.'

"Paulson & Co. is run by John Paulson who reaped billions by betting against the mortgage market to heavily influence which mortgage to include in an investment portfolio, while telling other investors that the securities were selected by an independent, objective third party,' Khuzami said in a statement."

Our readers will be left, as are we, with the conclusion that Paulson & Co. have purchased immunity on that count by providing evidence against his former colleagues.

However, be that as it may, the SEC deserves our applause for however long it took to seek out the details of Goldman's villainy peddling subprime collateralized debt to clients while making heavy bets through insurance that the investors they counseled for a first good profit, would lose their shirts to them as they bet heavily through insurance that the value of the same shares would collapse.

A key vehicle of the financial villainy that has brought the world economy to its current crisis consists of the use of derivative techniques.

These deal in rates of growth driven to unlimited powers to bring into the prevailing economic theory naively and ever seeking to maximize profits on a "pure and perfect market." In fact, at the very time that the SEC has taken its laudable if belated initiative, the stock markets of New York, Toronto, and other major financial centers, having lost much of their conventional business, are investing heavily in split-second trading facilities made possible by new technologies that pick up trading information from the Internet trading, seek out interesting patterns and formulate ways of betting against them. Often this is without even owning the stocks involved.

Purloining and Selling Advance Knowledge of Others' Trades

More than that, the access that these split-second trading centers will for a consideration sell to whoever will pay for the information even the proportion of buy and sell orders before they are executed, so that they can direct their private gambles from such information culled in advance. That is why those engaging in this latest twist, choose their offices close to more conventional trading center to be able to intercept details in trading patterns from the Internet, analyze them for useful patterns of other investors' intentions and move to a quick profit from that purloined advance knowledge.

Clearly what has resulted from these high-tech developments requires something far more alert and elaborate than SEC's response to date.

Most important is a knowledge of history. What we learned to make good use of from the years of the Great Depression, we have been systematically deprived of since the mid-1970s.

Canada had nationalized its central bank, the Bank of Canada, that had been established as a private institution in 1935. It did so by buying out some 12,000 share-holders at a good profit. That permitted Canada to finance its part in WWII more inexpensively than either the US or Britain, and then go on to absorb millions of mostly penniless immigrants to achieve a rate of prosperity unknown before.

These are days of ever-higher technology. Let us, however, start with technology at its lowest possible level: the rules of logic. You cannot turn around a relationship as though it were a pancake, and assume that the inverse is as valid as the original. If I shoot myself in the head, I fall dead. However, the inversion of that relationship is not necessarily true, If I fall dead, it is no proof that I killed myself. It could have been heart failure.

Yet that first rule of logic is being violated every day by our government and in the economic courses taught at most universities.

If prices rise, it might indeed to be due to real inflation, i.e. there is more demand for goods than can be supplied. *But prices can rise for quite different reasons.*

I looked into that important relationships in the 1960s and came to the conclusion that though an excess of demand over supply – which is real "inflation" will tend to drive up prices, the converse may have nothing whatsoever to do with a shortage of goods to satisfy demand. It could be due to quite other causes: the rapid urbanization going on in almost every country of the world which requires every costlier infrastructures, the more elaborate technology that calls for more education for most workers.

I first became aware of the vital difference between the first and the latter cases of rising prices, and sent out my manuscript to some 30 economic publications throughout the world. It was purchased and published in the leading French journal on economic theory at the time, *La Revue Économique*, and published over 70 pages in its May, 1970, issue. In it I used the term "social lien" to denote higher prices due to structural causes rather than a lack of supply to satisfy market demand. It was reviewed most favorably in at least eight economic publications including twice in the *Economic Review* of Cambridge University in Britain. In one of these, the author was particularly drawn to my title for the new factor that I recognized to designate the very different rise in prices due to greater costs for infrastructures provided by the government rather than marketed – "the social lien."

But today we are back to identifying any increase in the price level with "inflation" and have chosen to ignore the possible structural social factors as responsible. One, of course, is the rapid urbanization in almost every part of the world especially where population has been increasing. These require both far more physical and social infrastructure than used to be the case. However, what is significant is the resistance of the ruling classes to recognize any alternative explanation to "inflation" as a cause of higher price level.

Either it has been dismissed as an "externality" to be disregarded, or described as "benign" inflation. And yet it should be evident that the ever greater importance of infrastructures, makes the capital investment by our governments ever more important.

If we recapture even the extent of the recognition of structural factors in our price rise, whether due to the growing extent of our government's investment in physical capital, or its investment in human capital, we would recognize that such investment is not mere debt, but a valuable capital investment without which our society could not function.

Add to this a return to the proper use of the Bank of Canada to finance the capital investments of government, and the crisis would be over.

Unfortunately, whenever there is a basic shift in the social group in the saddle, the principles of good government – not excluding its accounting principles, when such actually exist, must change. If the personnel who ran the earlier shows remain in positions of power, you can bet the government's bottom dollar that the reorganization of the government's accountancy and hence tax policies will be blocked and rolled back. That is why the Obama government being tethered to a previous high government official is a sign of craven surrender.

We refer our readers to the further contents of this issue to grasp why our government, like that of the US, has some heavy lifting still to be done.

Bridge of Sighs

Once society crossed that bridge to the allegedly self-balancing market, humanity was headed for disaster.

It was only after my essay was published that I came to understand why. *La Revue Économique* had responded to my submission so quickly and generously. It was the mouthpiece of a remarkable group of French economists and economic historians who had been working along lines very related to what concerned me. On its editorial board was not only the great French economic historian, Fernand Braudel, but two statistical analysts who over different periods of time and place had compared price movement and the relation of supply to demand and found a discrepancy between price movement and the supply-demand relationship. This they had attributed to a factor quite different from market balance that still awaited identification. And at that point the postman brought my essay, miraculously filling the void puzzling them.

This brought me into contact with the French economist who was undoubtedly the most original economist in France at the time, François Perroux. One of his brilliant insights is what he termed the "dominant revenue" – the revenue of the class in the saddle that is taken for a reliable index of well-being of society as a whole. In Britain, during and after the Napoleonic wars, it had been the revenue of the land-owners who behind high tariff walls screwed up their urban and rural rents, and leased rather than sold their lucrative land holdings. But with the introduction of James Watt's steam engines into British factories, the "dominant revenue" passed to the industrialist who favored free trade that not only produced cheaper foodstuffs that allowed them to depress their workers' subsistence wages further, while resisting the protectionist pressures in Germany and the United States to resist the intrusion of the British industrialists interested in exploiting their monopoly of steam power while it lasted.

But before long a new menace appeared not on the misty horizon, but at the very center of society. Up to then economic theory had, in one form or another, been based on the amount of "average labor" entering the production of a commodity. With the replacement of mere human muscle with James Watt's steam power, the "dominant revenue" as advanced by Perroux shifted from land rents to the factories. This was formalized with the removal by Britain of her high tariffs to become the missionary of free trade at home and abroad.

So long as the British workers remained illiterate, they were unable to follow the discussions of the economists about the merits of various versions of the labor theory of value. However, in the fullness of time, British workers were learning to read and make disturbing deductions from the attribution of wealth creation to the quantity of labor that entered into its production. That danger became a major concern because of the flocking into Britain of thousands of socialist and anarchist leaders defeated on the barricades that had been thrown up in most continental lands. These refugees included Karl Marx and his family who lost no time in organizing open-air meetings questioning the existing social system almost within earshot of Buckingham Palace. Obviously the time had come for a very drastic revision of what Perroux called the "dominant revenue."

It arrived as though on schedule as the independent initiatives of at least three economists, working quite independently in several European capitals. This shifted Perroux's dominant revenue from the producers to the consumers and related it to the degree of pleasure purchasers derived from consuming a given product. It resolved with elegance the knottiest problems, e.g., mass unemployment. By this new enlightenment unemployment simply doesn't exist. What was mistaken for it was seen as the decision of the allegedly unemployed, after com-

Public Financing for Public Debt — A Challenge for the NDP

Canadians paid over $62 billion or $170 million per day in 2008/09 in unnecessary interest on federal, provincial and municipal debt. For 2009-10 the federal deficit will amount to $53.7 billion, which does not include provincial and municipal deficits. These costs are reflected in taxes, fees, cutbacks in public services such as education, Medicare, employment insurance, day-care and pensions and deterioration of infrastructure such as roads, sewers, water lines and affordable housing.

If our government had been using its own Bank, the Bank of Canada, as it should have for the past 35 years we would not be in this situation. From 1867 to 1974 the accumulated federal debt amounted to $18 billion, and during that time we paid for two world wars and other smaller ones, built the trans-Canada highway, contributed to construction of the St. Lawrence Seaway, built housing, provided funds for our veterans to go to school, brought in the Canada Pension Plan and made Medicare a national service.

In 1974 the government, which had been borrowing from its own bank since 1938 at near zero interest, decided to borrow less from there and more from the private sector at market rates of interest. *It also decided to allow the Bank of Canada to fight inflation by raising interest rates rather than increasing the reserves it held.* When interest rates went up the result was a huge increase in federal debt from $18 billion to $588 billion in 1997, with a total debt for all levels of government of over $900 billion.

In 2009 federal debt stood at $464 billion, but by 2015 it will be up to $635 billion. Federal debt charges, currently at $31 billion, will grow to $41 billion and based on previous figures the total debt charges for all levels of government will be about double the federal charges, i.e., $82 billion or $225 million per day. This is a huge burden to leave for our children, grandchildren and their offspring besides which the government uses the debt and interest costs to "justify" their cuts to public services.[1]

Economists tell us there are only three ways to reduce the deficit: grow the economy, raise taxes or cut expenses. We could cut back on public services such as health care, education, housing and infrastructure. That would save a bundle, but it would also make life for most Canadians much more difficult. BUT WAIT! Instead of cutting services we could cut interest paid on the public debt. The federal government can do this by borrowing from its own Bank at near zero interest, and to prevent the creation of too much money it can bring back the statutory reserves which had been removed by the Mulroney government in 1991/92. This would lead to a reduction in the profits of the commercial banks and less income for holders of government bonds, but the effect on most Canadians would be minimal.

When the government borrows from the Bank of Canada, any interest paid to the Bank is returned as dividend minus a tiny amount for administration. It's a virtually interest-free loan. So why does the government of Canada borrow from the private sector and pay interest instead of borrowing from its own bank? Besides the cost of the interest, borrowing privately *leaves the government vulnerable to the demands of its creditors.* Mackenzie King, Canada's longest sitting prime minister, understood the danger in this and stated in the 1935 election campaign:

"Once a nation parts with the control of its currency and credit, it matters not who makes that nation's laws. Usury, once in control, will wreck any nation. Until the control of the issue of currency and credit is restored to government and recognized as its most conspicuous and sacred responsibility, all talk of the sovereignty of Parliament and of democracy is idle and futile."

The government is in debt up to its eyeballs. It is afraid to do anything which might result in higher interest rates or cause some large corporations to invest their money someplace else, so it bows down to the money interests and slashes public services. To regain control over the issue of credit requires politicians who will talk openly about it and promote use of the Bank of Canada to carry public debt as well as reinstatement of the statutory reserves.

Many people are afraid that an NDP government would raise taxes to pay for their proposals, so they don't vote NDP. But it doesn't have to be this way. By using the Bank of Canada to carry public debt an NDP government could finance its proposals without raising taxes.

The NDP is spinning its wheels and is stuck in third place. To get out of this rut it needs to bring the issue of public financing for public debt out into the open. It's not a new issue. The CCF made it a fundamental part of its constitution in 1933, Tommy Douglas spoke of it, and a resolution in support of it was adopted at the NDP federal convention in 1995 – then ignored. Those opposed to public financing will fight very hard, ridiculing the NDP, challenging the concept, raising the fear of a loss in the value of our dollar.

The NDP will need to be very well informed on every point, get the support of as many experts as it can and plan ways to counteract the inevitable criticisms. There are those who are justifiably hesitant to embark on this road, but it isn't good enough to say there isn't enough community understanding of or support for this issue, or we don't know enough about it. The figures in this letter are enough to show that action must be taken. There are many who would offer their understanding and their expertise, but it first requires acknowledgement that the status quo is not acceptable and a willingness to act.

Richard Priestman

1. The five-year forecast as part of the Government's medium-term economic plan shows deficits of $53.7 billion in 2009-10, $48.9 billion in 2010–11, $28.7 billion in 2011–12, $20.6 billion in 2012–13, $12.5 billion in 2013–14 and $6.6 billion in 2014–15 were projected. Total of deficits comes to $171 billion which, added to the $464 billion in 2009, will bring the federal debt to $635 billion by 2015. (Department of Finance Budget Plan, Chapter 4.2)

paring the degree of pleasure they would derive from leisure in their parlors with the enjoyment available from work at the wages offered. And, of course, the leisure-in-their-parlors won out.

Such is the "dominant revenue" model that currently rules the world.[1] In any serious science, when two similar causes are found to have different effects, special care is taken to devise different names to distinguish the two divergent relationships. Otherwise it is impossible to develop the distinct chain of consequences by investigating where the disparity might lead. In official economics today exactly the contrary course is followed – all rising prices have continued to be designated as "inflation," and instead of changing the old terminology, it is the university faculties that have been subjected to the big broom, with those who have made use of the new discoveries being given early retirement or worse.

And yet it requires a mathematician to explain to our rampaging speculative bankers what can be insured no matter at what high rates depending upon the risk involved. However, what is not risky, but wrong – say 2 + 2 = 5 – cannot be insured. Insure it and the insurer or the insured, more likely both will likely end up bankrupt. And what appraisal companies are qualified establish the quality of such "investments"?

And how can a purported great "reformer" like President Obama choose as adviser a high official in the Treasury and Federal Reserve that led to the current mess? Unless there is a drastic change of both personnel and institutions, to support the doctrines of a reformed world, we will be heading into ever tenuous overblown gambles of which the new split-second trading is a good example. For years the phenomenon of ever-more leveraged hedge-funds was a sacred subject no more subject to question than the Virgin Birth, or the split-second trades on- and off-record are today.

The only certainty: government policy is headed is towards the ultimate gamble – atomic war. That is why we must fight for the liberation of our universities from the crushing silences imposed on them. They must help us mobilize our historical experiences, the resources of the mathematics and other scientific faculties so that they may provide objective appraisals of what has come to pass as economic policy. There is enough public indignation about the official economic polices and where it is leading us, to support the freedom of our universities to equip our world with adequate appraisals for what passes as serious policy to defend our society and its future.

William Krehm

1. Thinking akin to Perroux's "dominant revenue" has been independently developed by the American sociologist Robert E. Wood, whose book, *From Marshall Plan in Debt Crisis – Foreign Aid and Development Choices in the World Economy,* is reviewed in *Meltdown*, Vol. 3, page 20: "As a sociologist, Wood excused himself for 'tackling a subject generally the preserve of economists, and to a lesser extent of political scientists. I have not felt that I have left my sociologist's craft behind. It has become apparent to me that foreign aid plays a significant role in shaping those aspects of the world that sociologists look at social equality, class structure, politics, gender relations, rural-urban relations, and so forth. My training as a sociologist has made me sensitive to structures behind processes that on the surface seem without rhyme or reason. It is time that economists availed themselves of help from other disciplines to tidy up the mess in their workshop."

In other words instead of a highly rigged, but allegedly self-balancing market, sociologists bring in far broader and more complex human considerations, that just a few years ago orthodox economists dismissed as "externalities.")

Bill Presented for Another Suppressed Lesson of History

The New York Times (5/09, "The Ghosts of Gandamak" by William Dalrymple) presents us with another of the main cuts of history of which we have been so disastrously been deprived.

"The name Gandamak means little in the West today. Yet this small Afghan village was once famous for the catastrophe that took place there during the First Anglo-Afghan War in January 1842, arguably the greatest humiliation ever suffered by a Western army in the East.

"The course of that distant Victorian war followed a trajectory that is beginning to seem distinctly familiar. In 1839 the British invaded Afghanistan on the basis of dubious intelligence about a nonexistent threat. Information about a single Russian envoy to Kabul, the Afghan capital, was manipulated by a group of ambitious hawks to create a scare about a phantom Russian invasion, thus bringing about an unnecessary, expensive and wholly avoidable conflict.

"Initially, the conflict proved remarkably easy and bloodless. Kabul was captured within a few months and a pliable monarch, Shah Shuja, was placed on the throne. Then an insurgency began which unraveled that first heady success, first among the Pashtuns of Kandahar and Helmand, then slowly moving northward until it reached the capital.

"What happened next is a warning of how bad things could yet become a full-scale rebellion against the British. It first broke out in Kabul, and the two most senior British envoys were murdered, making the British occupation impossible to sustain. On the disastrous retreat that followed, as many as 18,000 East India Company troops and perhaps s many as half again Indian camp followers (estimates vary), were slaughtered by Afghan marksmen waiting in ambush amid the snow drifts and high passes, shot down as they trudged through the icy depths of the Afghan winter.

"The last 50 or so survivors made their final stand at Gandamak. As late as the 1970s, fragments of Victorian weaponry could be found lying around in the screes above the village; even today the hill is covered with bleached British bones. Only one man, Thomas Souter, lived to tell the tale. It is a remonder of the increasingly pertinent parallels between the events of 1842 and today's that one of the main NATO bases in Afghanistan is named Camp Souter.

"For the Victorian British, Gandamak became a symbol of the country's greatest imperial defeat, as well as a symbol of gallantry: William Barnes Wollen's celebrated painting of the Last Stand of the 14th Foot – a group of ragged but determined British soldiers standing in a circle behind their bayonets as the Pashtun tribesmen close in – was one of the era's most famous images.

"For the Afghans themselves, Gandamak became as symbol of freedom, and their determination to refuse to be controlled by any foreign power. It is again no accident that the diplomatic quarter of Kabul is named after the Afghan leader who oversaw the British defeat at Gandamak Wazir Akbar Khan.

"A week ago, while doing research for a book on the disaster of 1842, I only narrowly avoided the fate of my Victorian compatriots.

"Gandamak backs into the mountain range that leads to Tora Bora and the Pakistan border, that has always been a Taliban center. I was trying to follow the route of the British retreat, but had been advised not to attempt to visit the Gandamak area without local protection. So I set off in the company of a local tribal leader who is also a sports minister in the Karzai government, Anwar Khan Jigdalek. A mountain of a man, Anwar Khan is a former wrestling champion who made his name as the mujaheddin commander against the Soviet Union in the 1980s.

In the Footsteps of Britain's Greatest Humiliation

"We left Kabul – past the blast walls of the NATO barracks that were built on the very site of the British cantonment of 170 years ago – and headed into the line of bleak mountain passes that link Kabul with the Khyber Pass. At Sarobi we left the main road, and moved into Taliban territory; five trucks full of Anwar Khan's old mujaheddin comrades, all brandishing rocket-propelled grenades, appeared to escort us.

"At Jidalek, on the 12th of January, 1842, 200 frostbitten British soldiers found themselves surrounded by several thousand Pashtun tribesmen. The two highest-ranking British soldiers were taken hostage. It was 50 of those infantrymen who later managed to break out under cover of darkness to make the final passage to Gandamak. Our own welcome was, thankfully, somewhat warmer.

"It was Anwar Khan's first visit to his home since he had become a minister, and the villagers treated us to a feast, Mughai style, in an apricot orchard. We sat on carpets next to bubbling irrigation runnels, under a trellis of vine and pomegranate blossoms, as course after course of kebabs and mulberry-scented rice were laid in front of us.

"It was nearly 5 pm before the final pieces of naan bread were cleared away, and our hosts decided it was too late to head on to Gandamak. Instead, we went that evening to the nearest big city, Jalalabad, where we discovered that we'd had a narrow escape: there had been a huge battle at Gandamak that day between government forces and a group of villagers and Taliban fighters. Our gluttony had saved us from driving straight into an ambush.

"The battle had taken place on exactly the site of the British last stand. In Afghanistan, imperial history seems to be repeating itself with almost uncanny precision.

"The following morning I attended a jirga, or assembly of tribal elders, to which the graybeards of Gandamak had come, under a flag of truce, to discuss what had happened the day before. The story was typical of all I had heard about the current government, and revealed how a mixture of corruption and incompetence had helped give an opening for the return of the once-hated Taliban.

"The elders related how the previous year, government troops had turned up to destroy the opium harvest. The troops promised the villagers full compensation and were allowed to burn the crops; but the money never came. Before the planting season, the villagers again went to Jalalabad and asked the government if they could be provided with assistance to grow other crops. Promises were made; again nothing was delivered.

"So, desperate, the villagers planted poppies, informing the local authorities that if anyone tried to burn the crop, they could have no option but to resist: they had children to feed. When the troops turned up, about the same time we were arriving at Jigdalek, the villagers were waiting for them, and had called the local Taliban to assist in the fighting that followed. We were told that nine policemen were killed' six vehicles were destroyed and 10 police hostages taken.

"Ever since, I have been thinking about the close parallel between that NATO now faces in Afghanistan, and that faced by the British more than 150 years ago. Then as now, the problem is not hatred of the West, per se, so much as a dislike of foreign troops ordering people around in their own country.

"There has always been an absolute refusal by the Afghans to be ruled by foreigners, or to accept any government perceived as being imposed on them. Then as now, the puppet ruler installed by the West has proved inadequate for the job: simultaneously corrupt and weak, and forced to turn on his puppeteers to retain a fragment of legitimacy in the eyes of his people.

"Then as now, there have been few tangible signs of improvement under the Western-backed regime: despite the billions of dollars sent to Afghanistan, Kabul's streets are still more rutted than those in the smallest village provincial towns of Pakistan. There is little health care: for any serious medical problems, patients have to fly to India.

"Then as now, the presence of large numbers of well-paid foreign troops has caused the cost of food and provisions to rise, and living standards to fall; Afghans feel they are getting poorer, not richer. Then as now, there has been an attempt at a last show of force to save face before withdrawal. As in 1842, this year's surge has achieved little except civilian casualties.

"It is not too late, however, to learn some lessons from the mistakes of the British in 1842. Then as now, the British officials in Kabul continued sending out dispatches of delusional optimism as the insurgent moved ever closer to Kabul. Those officials believed there was a straightforward military solution to the problem, and if only they could recruit enough Afghans to their army, they could eventually march home and leave the pliable regime in place. By the time they realized they had to negotiate and reach a compromise with their enemy, their power had ebbed too far, and the only thing the insurgents were willing to talk about was unconditional surrender.

"Today, too, there is no easy military solution to Afghanistan: even if we proceed with the current plan to spend billions equipping an Afghan army of half a million troops, that force will never be able to guarantee security or shore up such a discredited regime. Every day, despite the military muscle of the US, the security gets worse, and the area under government control contracts.

"The only answer is to negotiate political solution while we still have enough power to do so – which in some form or another means talking with the Taliban. Otherwise, we may yet be faced with a replay of 1842. George Lawrence, a veteran of that war, issued a prescient warning in *The Times* of London just before Britain blundered into the Second Anglo-Afghan War in the 1870s. 'A new generation has arisen which, instead of profiting from the solemn lessons of the past, is willing to and eager to enthrall us in the affairs of that turbulent and unhappy country,' he wrote. 'Although military disasters may be avoided, an advance now, however successful in a military point of view, would turn out to be politically useless.'"

However, the West, in any country you might care name has achieved the miracle of trying to run our lives and our economies by completely suppressing what we had learned from any historical or scientific discipline you would care name – history logic, sociology, health care, accountancy, meteorology, you can go on ad infinitum. It is all replaced with self-balancing supply and demand. How then are we to be guided by a remote land that sent Alexander the Great packing up and getting out in good time? And there are gobs of necessary principle to cope with the illiteracy imposed in almost anything that you might name. We deal with some of these in the rest of this issue.

W.K.

Retesting the Globalization Model

On rereading the volumes of *Meltdown, Money, Debt and the Wealth of Nations,* an anthology of articles from our monthly magazine now in its 22nd year, I am shocked by the systematic way in which governments throughout the world have turned their backs on just about everything essential for avoiding the world's present troubles.

Section One

I will quote from Volume 2 of *Meltdown*, published by COMER from the material carried in its monthly magazine for the last 22 years. It appears on page 174, from an article "Testing the Globalization Model."

"The world has been launched on a course of absolute free trade and virtual diplomatic passports for speculative finance…. Not only all barriers, but even speed bumps are being done away with. No one has ever been over this route before. The only ground for believing that it will bring peace and prosperity to the world is an academic model of the 'self-balancing market' that assumes all actors of such trifling size that nothing they do or leave undone individually can have the slightest effect on price. That in itself is basis enough to qualify the economic theory taught in our universities [today] as religious faith or plain charlatanry.

"But, above all, the present globalization is not working. It has led to the emergence of a single economic and military superpower. This is the very antithesis of the infinitesimally tiny actors postulated by marginal theory. And on which the reasoning was based. That contradiction is turning up not only in spreading discontent – the mass demonstrations against the globalization conferences in Seattle and Washington, DC, the outbreaks of civil wars, but in the drop in life-spans in Russia over the past decades, the overcapacity in industries such as motor vehicles, the deepening trouble in financial institutions on all continents, the crushing load of consumer debt that precariously sustains the boasted prosperity of the lone superpower.

"All this could have been foretold with the help of some simple reasoning requiring only a pencil and paper. All we needed was the history of the 1930s, plus some elementary rules elaborated by non-conventional economists, or readily adapted from other better-grounded disciplines.

"Let us mention some of these.

"Test One. The Tinbergen Counting Theorem. Some decades ago a Dutch economist Jan Tinbergen, originally trained as a physicist, tried injecting some scientific method into economics. In our first-year of high-school algebra we learned that if two independent variables can be identified in a problem, the solution must have two variables. One won't do. If three independent variables exist in the problem, the solution must have three independent variables, and so forth. This came to be known as 'Tinbergen's Counting Rule,' once honored by economists in the abstract, but rarely used.[1]

"Let us apply it to 'globalization.' The more barriers to trade and the free flow of capital you remove, the greater the number of wild cards in the economic debt. New independent variables unleashed overwhelm us. For example, allow the free flow of speculative capital, and exchange rates will become a gamble, which according to the free-trade doctrine, can only be countered by higher interest rates. But higher interest rates ransack the public treasury for the benefit of usurers, and bankrupt the economy. That unleashes social unrest which overwhelms us with an entire Pandora's box of problems, each with its own independent variables. However, the free-market model which is supposed to justify and control all this consists essentially of two independent variables: 'supply' and 'demand.' By the Tinbergen Test, globalization as an overriding goal strikes out right there."

New Variables Sprout in All Economic Subsystems

"The number of independent variables in our technologically driven economy is not only open-ended, but their number is ever increasing. Only systems theory that tracks these independent variables and the subsystems that arise around them can equip us to handle the resulting problems. There are two constraints to be observed. Each subsystem has its own distinctive code, and no subsystem must be cannibalized by another. The functioning of the whole system requires that each subsystem be kept in working order. An example of such a system is the automobile. It consists of a set of subsystems – the chemical (fuel), the electromagnetic, the electronic, the mechanical. If a single one of these ceases to perform, the car cannot move safely.

"What we call the ecology is actually a complex of different subsystems. Each type of pollution – greenhouse gasses: mercury pollution of our water supply, bacterial pollution of various sorts, has its own limit of tolerance. Averaging them out won't do. Since every subsystem must have at least one independent variable, keeping up with the economy must be recognized as a dynamic, ever-evolving affair. Running it with an eye on two flawed variables – market supply and demand – cannot possibly do the job. The assurance that it can is deduced not *by* but *from* a device in calculus over a century ago is an absurdity.

"The next test I have called the 'Gaussian.' It has not been used by economists before, although it does play an important part in our daily lives. Karl Friedrich Gauss was the greatest mathematician of the 19th century. His concept of the 'modular congruence' subtracts the highest multiple of a given modulus from two or more functions that we are concerned with, and deals only with the remainders. Thus we name the days of our week to modulus seven – after coming to the end of the week we start against with Sunday. Without this intuitive ancestral use of modular congruence, we would have gone on giving a new name to every day since the birth of Christ. That would have hopelessly complicated our lives. The equivalent of that turns up in our economic policies.

"The only vague allusion to such a test among economists that comes to my mind before the development of systems theory a couple of generations ago, is John Maynard Keynes's remark: 'Why send cookies from Denmark to Britain and vice versa? Wouldn't it be simpler to exchange recipes?' Globalization multiples needlessly the mileage chalked up on land, sea and in the air, with attendant congestion and pollution. The additional costs go to swell the GDP and this is reckoned mistakenly as an increase in our productivity and well-being.

"However, the applications of Gaussian modular congruence must be extended to every area of the economy. In fact, economists of the third millennium must be redefined largely as practitioners of modular congruence. Since the number of independent variables and hence of subsystems in the economy is ever growing, the scope and need for such Gaussian trade-offs will go on climbing. Recognizing this multiplies the options for helpful policy design.[2]

"Let me cite a simple example. For the last thirty years governments have been preoccupied primarily with 'licking inflation.' But monetarist orthodoxy has reduced the means of achieving this to raising interest rates. That, however, increases the financing costs of the state and shrinks its revenues at the same time. That plays havoc with the solvency of both the state and the [private] economy.

"The Gaussian solution would be to work out schemes that would point these two parameters downward – one affecting the revenue of the state and the other its spending – in equal degree. Accordingly, the direct effect on the two on the treasury would cancel out. Their indirect effects, however, would benefit the economy as a whole and spare innocent parties from 'friendly fire' of misconceived policy."

Tax-bonds — An Example of Gaussian Congruence Policy Design

"In 1977 I first proposed 'tax-bonds' as an instance of policy based on modular congruence. Certain classes of taxpayers would be granted the option, rather than paying taxes on a portion of their taxable income, to invest it in long-term 'tax-bonds' yielding a rate considerable less than the market. Its lesser rate would not *defer* taxation but *replace* it. That would decrease both the revenue of government, but also the interest paid on its debt. Both these items could be calculated to balance each other, so that their direct effects on the fisc would cancel out. And the benefits of lower taxation and lower average interest rates on the entire economy would be wholly a bonus.

"A hedging feature could be included. Over the longer term the growing portion of the public sector within the economy leads to an upward structural gradient. Together, the lower taxation and lower interest-rate will attenuate this. To the extent that they do, the government will have achieved a lower price level without resorting to higher interest-rates. This is likely to result in the shrinkage of the real value of the principal of the tax-bonds when redeemed.

"Since that was originally written, a highly timely insurance feature can now be incorporated into the scheme…. There could be provision for the resale of the tax-bond to the government in the case of a serious lengthy illness in the vendor's family, long, involuntary unemployment, or the death of a breadwinner.

"The pursuit of globalization leads to a harmful congestion not only of geographic, but of economic and social space. The aggressive market logic, without basis in contemporary or historical reality, encounters ever new independent variables in needless mileage run up and the congestion of both geographic and economic space. The Tinbergen test is being violated to the very disaster point.

"What we are now proposing is a double dosage of Gaussian Policy design: 1. Lower debt assumed by the government; 2. A prepaid health insurance feature in return for a further lowering of interest rates on special bond issues with that feature.

Why the Closed-mind Syndrome by Governments and Universities to Simple New Policy Design?

"That question introduces another vital factor. Who benefit from the persistent perversity in eradicating just about everything the world learned about converting raw capitalism into a more people-friendly mixed economy? Obviously, speculative finance benefits from globalization, from wholesale privatization, deregulation, regressive taxes and user fees, the suppression of the defenses of domestic economies, from revolving-door facilities for quick entries and getaways for footloose finance. What is at stake is something that free-market theory denies the existence of – the factor of raw power that could hardly exist without the ability to impose a belief system to make the current 'globalization' possible.

"That power has emerged in all its nakedness with the crumbling of the Soviet Empire which in certain areas, by its very existence, exercised a certain restraining balance. What has occurred since the disappearance of the rival superpower resembles an overwhelming flood when a dam collapses. To properly appreciate what has happened, the 'dominant revenue' concept of the late, great French economist, François Perroux, is indispensable.

"Note how perfectly Perroux's definition of the 'dominant revenue,' published in 1966 before the phenomenon had reached full power, captures the present situation.

"The European Occident has passed through successive periods of development, each characterized by a typical morphology of distribution and by a dominant revenue. In turn the dominant revenue has been that of the landowners, then industrial profit, then financial and industrial profits in a mixed economy, in which the rate and mass of profit are functions of a complex combination of public and private, of market and extra-market actions.

"During a specific period of development, the dominant revenue is the one to which the others adapt themselves. In an apologetic doctrine, it is presented as the revenue that, by the rate and mass which it achieves, determines whether the given economy functions properly. In the institutional framework corresponding to the given dominant revenue, that in fact is the case; but in another context it would be otherwise."

"That provides us with yet another vital test in assessing policy. Rather than accepting the bare assertions and promises of official economists, we must ask whom a given measure profits. Right from the beginning we must check for conflicts of interest. To declare interest rates the one stabilizing tool is an outrage. Accept it, and there is no way of disentangling economic policy from the interest of speculative finance.

"The very nature of economic theory stands in need of rethinking. Now that the globalization model is patently failing, putting it to such basic tests will be an important step towards that goal.

The Key Relevance of Gaussian Modular Congruence

"We must learn to do our reasoning in terms of net effect; we must train ourselves in the methods of modular-congruence arithmetic.

"When two functions are congruent to modulus k, their difference is made up of a multiple of k plus the same remainder. That is written $f(x) - g(x) \equiv \text{mod:k})$. They are each made up of a multiple of k plus the same remainder. In his calculus the common remainder alone is of importance.

"Applied to economic reasoning, modular congruence would focus on the net effect of two inverse operations. It would establish that only the net effect of our efforts is likely to be useful.

"Thus, whatever the quantum of public services delivered, it is desirable that the fiscal turnover be kept to a minimum. A policy format in which the state taxes an industry with one hand and subsidizes it with the other is burdensome. Taxing and subsidizing at the same time must be seen as similar to running a heating system against an air-conditioner."

Underlining the Irrelevance of Monetary Theory

"Marginal theory was crafted towards the end of the 19th century to present a world torn by social discontent in the best possible light. All parties in the economy were viewed as just traders. Each studied the price of the last sale of whatever he had to offer and decided whether it would increase his satisfactions making or not making the sale, be it of bond issues, railways or just labor power for digging coal. With everybody thus redefined as just traders, the market became coterminous not only with the economy, but with society itself. No need worrying about the horrors of the work place, so dramatically portrayed by Emile Zola. Automatically the market would take care of all that sordid stuff, and it could be left to Cambridge dons to work out the details. Economics was reduced to one great euphemism that could keep social discourse polite if irrelevant.

"Early in the history of this new doctrine, certain difficulties arose in linking it, no matter how remotely, to the real world. To apply differential calculus, which was the purpose and the technology of the operation, producers were assumed of such negligible power and size that nothing anyone of them did or left undone could possibly affect the market. They had no information other than the price of the last sale. And they went on producing until they just broke even on the last unit sold. But how did they determine that they have earned neither a profit nor incurred a loss on the last unit sold? And soon enough to go on with the exercise? Leon Walras who gave marginal utility its most rigorous mathematical form, got around that little problem with panache.

"He had his traders 'cry' their wares and conclude provisional transactions at provisional prices ('bons'). For these provisional prices they receive provisional certificates ('bons'). But once the last sale has been made and the true 'break-even' price has been established, all previous sales were adjusted to this final price. (*Elements d'économie politique pure*, Lausanne, 1900, p. 213).

"But why bother with such notice. For good enough reason. It is built into the genes of our 'leave it all to the market' thinking and inevitably, unless exposed and uprooted from the model must show up in the most advanced high-tech patterns of our business world today."

This should be a matter for much reflection A theoretical dreamer, unconsciously seeking to structure the concept of an automatically free and just market actually anticipated the criminal practice of "kickbacks" that receives so much attention from the law courts today.

We quote *The Wall Street Journal* (8/11), "How shifting Prices in PC Business Undid Top Dealer Inacom" by Gary McWilliams: "The final chaotic hours of InaCom capped one of the wildest rides in PC history. During and industry growth spurt in the 1990s, the Omaha company gobbled up rivals, becoming a Goliath with $6.9 billion in revenue. It supplied PCs and revenue services to a third of America's biggest companies.

"But as PCs changed from an adolescent business to a mature one, Inacom was left by the wayside. Several large PC makers, trying to match Dell Computer Corp.'s astonishing direct sales success, created a Byzantine two-tiered pricing system that crippled longtime partners such as InaCom.

"Inacom found itself in a tangled financial mess. Its auditors never signed off on its 1999 numbers or on a restatement of its 1998 results."

Columbus was a Piker, Crossing Only a Single Ocean

The Wall Street Journal (29/1, "Winnick's Lavish Ways Matched His Big Ambitions for Global Crossing" by Deborah Solomon and Anna Wilde Matthews, sketches the corporation and its creator: "Gary Winnick's dreams for Global Crossing knew no boundaries in 1997 at the e-com upstart's first sales meeting. The company he founded was selling capacity on its trans-Atlantic fiber. As he watched the eager recognition. Mr. Winnick took a piece of yellow legal paper, taped it to the wall, and scrawled on it a globe with lines connecting the various continents. Global Crossing would offer fiber throughout the world.

"No preliminary research of effective demand, or timing were required. The difference between future and present had simply been erased. Balance sheets were parted, as the Lord Himself had the land and the waters, night and day. Future assets lit up the balance sheets, while liabilities crouched demurely under the table.

"With Enron it was mostly partnerships, off balance-sheet, that turned out to be private fiefs operated by Enron officials. By the time Global Crossing filed for bankruptcy early in February 2002, its stock had fallen from a $64 high in 1999 to 30 cents a share. As a by-product of the bankruptcy procedure, for the first time the truth of how GC's financial wizardry was achieved emerged.

In the *WSJ* ("Optical Illusion: Global Crossing Used Swaps to Enhance Its Revenue: It Wasn't The Only One" by Dennis K. Berman and Deborah Solomon) delivered some details: "Analysts are scrambling to decipher accounting practices of scores of telecom companies to figure out whether other bombshells are lurking.

"'It raises the question whether companies are creating real economic revenue or sham transactions,' says Lynn Turner, former chief accountant at the Securities and Exchange Commission between 1990 and 2001. At the center of the debate is a type of lease known as an Indefensible Right of Use. Pioneered decades ago when AT&T Corp. was still a monopoly, such leases allowed competitors to gain access to the costly undersea cables that only Ma Bell could afford to build.

"Today, so-called IRUs allow a telecom carrier to buy all types of telecom capacity and gear at low rates, typically for periods of 20 or 25 years. Since IRUs are technically rights to a physical part of an underground cable, they can be considered an asset. That means their cost isn't part of a company's operating results, but of the property plant, and equipment line listed on a firm's balance sheet.

"The transactions under scrutiny work like this: Company A sells an IRU to Company B and books the incoming cash as revenue. Meanwhile Company A buys a different IRU from the same Company B, and treats the transaction as an asset purchase, which doesn't affect financial results that excluded interest, taxes, depreciation, and amortization, and in some cases were used to secure debt financing. But some accounting experts now question that approach, saying many such transactions would more properly be recorded as straight exchanges of assets, which restrict a company's ability to book revenue.

"Several companies have acknowledged booking revenue through capacity swaps – often through deals with Global Crossing. Qwest Communications International Inc. and 360 Networks Inc.… One such transaction was treated as investment, the other, though identical, as income. What it received over the years for what it sold could be discounted for present value to show more net worth and as collateral for loans."

I could continue for many months examining the aggressively economic models directed to wipe out even the memory of key legislation, our history, every possible attainment of economists and sociologists to restore the absolute domination of the aggressive speculative banking that has already brought on the current crisis. But at this point I must pause and pass directly to the prepare the ground for assessing the Greek crisis that threatens to spread throughout the European Union and far beyond even to the Canada.

For that I must revert to some dearly purchased lessons that we had already learned but have been wiped out of official and even public memory.

The Most Important Lesson to Come Out of World War Two

At the end of World War Two, Washington lost no time in sending many hundreds of American economists to Japan and Germany to study the war damage and predict how long it would take for the two leading axis powers to become again the formidable trading countries that they had been. Some sixteen years later one of these, Theodore Schultz, published a book in which he explain how and why he and his colleagues had been so far wide of the mark. They had concentrated on the physical damage suffered by Japan and Germany and paid little attention to the fact that the skilled work force, technologists, and scientists had come through the struggle almost intact. From this Schultz concluded that investment in human capital, education, and hence health, and security is the most productive investment a government can make.

That should have surprised no one. The so-called "spending" for education, and hence for health, social security, and the environment rather than just "spending" has the features of a further investment. The children of educated parents tend to be more readily educated, healthier, with a greater sense of security. Britain is still getting returns on whatever the town of Stratford-Upon-Avon spent on teaching Billy Shakespeare the glories of the English tongue and the folly of men.

For a few years Theodore Schultz was celebrated for his inspired conclusion, and even awarded a Nobel Bank of Sweden Prize. But in no time at all he has been buried in oblivion, rather than just "forgotten." It was not an insight – precisely because of its stunning importance, which could be tolerated if the "dominant revenue" of our day – speculative banking – is to score a comeback. The latter has already equipped itself to attain through the split-second trading facilities in and off public exchanges being set up internationally.

RENEW TODAY!
(SEE PAGE 2)

That is why the stroke of genius of Theodore Schultz has been deliberately buried when it is most critically needed, has become of key importance.

It is the unmentioned issue in the great explosion of indignation and the difficulties in funding the debt of Greece.

Before we are able to talk about the debt of any government, but particularly about Greece, we must have a meaningful system of accountancy to tell us what is debt and what is simply wretched accountancy. The discovery of the Americas and of the maritime route around from Europe to Asia was made possible by the Order of the Templars, who brought back from the Holy land accrual or double-entry accountancy developed in Muslim lands. There this had been invented to make sure that interest was not being charged to an enterprising merchant unless the lender shares the commercial risks of the voyage with the merchant who usually accompanied his goods. Under this system every transaction was entered twice – one the cash or credit invested in the undertaking – that was "amortized," paid off "to extinction" according to a preset schedule. On the credit size was the current market value of the enterprise and that was "depreciated" marked to value (from the Latin *de pretio*). That made possible the voyages taking years to complete that led to the discovery of the Americas while in search for a west-going route to Asia and to the east going one around the Cape of Good Hope. It also made possible the financing of lengthy wars that served to consolidate local principalities into major kingdoms.

Accrual accountancy made possible the unique success of the Venetian Republic that was able to trade with Muslims and welcome Jew. Protestant and Muslim without persecution within its city.

That makes it more scandalous that the great conclusion of Theodore Schultz should have been forcibly buried and human capital is still not being entered into the ledgers of our governments. Were that done, the debt of all governments, but particularly that of Greece would appear as a most productive investment prepaid largely in advance, with a rate of return that would make an investor delighted.

But then, too, there is the voracious demand for renewed and expanded infrastructures in this day of accelerating urbanization.

I had not visited Athens for some thirty years, and I was astounded to see how that city had developed beautifully with new museums, galore parks while growing some tenfold in population. That was not wasting capital but making an investment not unworthy in the great land to whose legacy we are so indebted. That is why I have chosen Greece to illustrate our point. For our debt to Greece is not just bad bookkeeping, but relates to our very cultural roots. For the grounding of our own literature, to cope with our own basic mental decline – for the sociologists who learned from Socrates and Aristotle that human relationships cannot be conceived as a just a relationship of buyers and sellers or whatever, but are essentially at least a three-way affair including the effects on society rather than a simple two-way buy-and-sell exercise. That merely brushes our cultural indebtedness to our Greek heritage, the failure to mention that debt should cause us to hang our heads in shame. If we amend our view of what we owe Greece and what Greece owes us – not excluding a likely degree of hanky-panky – that will arise when debtors justly or unjustly get into trouble.

We should offer Greece more than a cup of hemlock. And if we do, we should remember that a just treatment of Greece in her great need will help the wealthier, bigger countries of Europe and the Americas put their own accounts in better order.

For since it was the large powers who decided to "globalize and deregulate" the world, they have a survival need for the wisdom of classical Greece. Much of what I have described in this paper would be covered by the Nicomachean Ethics of Aristotle.

We hear a lot about tax-evasion in present-day Greece. They too must update their grasp of their country's timeless gift to the world, just as Britain might recognize the importance of returning the Elgin marbles. And to "sell" the deal, as the saying goes, Greece can offer special rates to the citizens of the countries that rise to the occasion when they come to visit their incredible museums that make that great little land in which the world must recognize its stake of indebtedness.

William Krehm

1. Krehm, William (1977). Babel's Tower – The Dynamics of Economic Breakdown. COMER Publications: Toronto.
2. Perroux, François (p. 958) Presse Universitaire de France.

En Route to the Ultimate Disaster

In the lead article our readers can read the incredible achievement of G.G. McGeer, the high-school drop-out who managed to reformulate the relationship between government debt that compelled recognition that investment in government infrastructure in both physical and human capital, more than pays for itself, and requires neither gold, silver, nor indebtedness to private banks.

In doing so, McGeer persuaded the prime minister of the day, Mackenzie King, to nationalize the Bank of Canada. The consequences of that equipped Canada to finance its part in World War II more economically than Britain or the US, and the assimilation of a huge influx of mostly penniless immigrants from Europe, and a tremendously successful transformation of the country's economy from a largely agrarian economy to a modern industrial one.

The details of that quite unique achievement, however, have been buried in oblivion, though still on our law books. The key importance of human capital, the most important lesson to have come out of WWII, is likewise forgotten in the interest of government-bailed out mega-speculative banks.

The importance of the work of McGeer, which has acquired such key importance in the present world economic crisis, appears from the report in *The Wall Street Journal* (11/05, "Europe Bailout Lifts Gloom" by Marcus Walker, Charles Forelle, and DavidVillars) shows how handicapped the world is with our history, and the work of generations of economist, sociologist, and physical scientists has been wiped out to keep the monopoly of parasitic speculative banking in command.

We come up against the detail that the central bank of the European Union was put together by an extreme rightist de Gauliste government in France. To leave the speculative banking interest in the saddle the governments of the central bank of the EU charged the member government interest in their financing of both physical and human capital investment, rather than being credited with their capital investment – whether physical or human. But let us quote the *WSJ:*

"Investors' apparent short-term relief was tempered by some economists' worries that in the longer term, the agreement's pledge to bail out the troubled members will saddle the euro zone with gargantuan debts.

"Stocks surged in Europe and the US after EU leaders agreed to a massive action to prevent Greece's financial troubles from spreading throughout the region.

"The euro, which has been battered in recent weeks, rose above $1.30 to the dollar before closing below $1.28. The Dow Jones Industrial Average rose 404.71 points, or 3.9% to 10785.14."

The World has Forgotten Its Cultural Debt to Greece

"European Union officials announced early Monday in Brussels a plan to support the euro zone with €500 billion that could be lent to imperiled member countries, with more available from the International Monetary Fund. The deal was the result of a marathon weekend session of European leaders – one that included lobbying calls from US officials, canceled trips and a collapsed finance minister. The plan quieted concerns that European leaders weren't moving fast enough to ease fears of a spiraling market panic.

"But the deal drew immediate criticism in Europe and the US. On Tuesday, Federal Reserve chief Ben Bernanke is set to brief lawmakers on the Fed's weekend decision to extend dollar loans to the European Central Bank. Some lawmakers have assailed the move as a bailout for Europe.

"Many economists warned Monday that Europe's radical rescue plan doesn't address the region's underlying economic weaknesses, and could undermine the euro zone's rules and institutions.

"Analysts warned that blanket bankruptcy protection from Germany, France and other core euro nations could even reduce pressure on profligate euro-zone governments to mend their ways.

"'This step was needed to calm financial markets, and it perhaps succeeded. But it opens fundamental questions about the monetarist union,' said Daniel Gros director of the Centre for European Policy Studies in Brussels. 'There may be no way to enforce fiscal discipline.'

"The sweeping measures mark a historic turning point for Europe's single-currency zone. Until now, its 16 nations have shared a single currency and unified monetary policy, set by the European Central Bank, while operating separate national budget and tax regimes.

"The weekend's negotiations put the bloc on a headlong course toward fiscal coordination – undoing some of the zone's founding principles, including its ban on governments bailing each other out. It raises questions, analysts say, about the independence of the ECB, having long been shielded from political pressures.

"The uncertainty about the euro zone's future governance makes it even more unlikely that the bloc will be willing to admit new members for the time being, especially since many Eastern European candidates have their own debt woes.

"German Chancellor Angela Merkel, bleary-eyed after marathon negotiations Sunday night, said euro-zone nations need to intensify efforts to cut budget deficits. She stressed that aid for euro-zone governments would come with strings attached.

"For Germany, the EU's biggest economy and paymaster, the aid package is a decisive affirmation of political and financial commitment to Europe. Yet that commitment was born out of fear that the euro could fall, rather than enthusiasm for deeper union. Ms. Merkel's challenge is to convince Germans of a course that could wind up leaving them on the hook for other euro members' debts.

"'This package serves to strengthen and protect our common currency,' Ms. Merkel said Monday. 'We are protecting the money of the German people.'"

However, it would be crystal clear then – had the very concept of investment so brilliantly presented by McGeer and a quarter of a century later by Theodore Schultz not been suppressed. It had resulted from a massive experiment by Washington after WWII sending hundreds upon hundreds of economists to study the war damage inflicted on Japan and Germany, and finding that they were wide of the mark for leaving out the detail that the human stock of those two great trading nations had come through the conflict relatively intact. It is nothing short of suicidal for humanity to allow this basic lesson on the importance of investment in human capital to be buried once again.

"The chancellor for months resisted pressure to bail out Greece, fearing a precedent that could undermine budget disciplines and saddle taxpayers with unpalatable burdens."

"The €750 billion package has three elements. A government struggling to refinance its debts could first tap a €60 billion EU emergency fund. If that proved insufficient it could borrow from a €440 billion fund financed through a special-purpose vehicle whose borrowings will be guaranteed by other euro-zone governments. Euro zone officials officially placed the IMF's pledge at €250 billion, but a fund official said Mon-

Distinguishing between Complexity and Corruption

This is famously a scientific age in which no scientific secret from the minute interrelations of living cells to the secrets of interplanetary space are analyzed and eventually solved. It is then remarkable that sovereign states should be stumped in an age when few responsible posts are filled without a doctorate degree from a notable university.

And yet in determining the solvency or insolvency of societies what is clearly missing is the use of beginner's algebra. It is that if a problem has two distinct variables, you need two different equations of the first degree to solve them. If there are four such independent variable you need four to solve it. If there are more independent variables you need four independent first-degree equation to solve your problem, It is most unlikely that with PhDs all around the place making profligate use of calculus in virtuoso derivative insurance of the uninsurable, that they have forgotten what used to be taught in the first week of first-year high school courses that every student had to take.

We are left then with the melancholy conclusion that it is not honest ignorance, but enforced forgetfulness to keep their jobs, if we must avoid the harsh term "corruption" that has taken over.

With that brief forward let us turn to *The New York Times* article (2/05, "It's Complicated" by David Segal): "Ladies and gentleman, the state of our union is stumped.

"The Great Recession and the wars in Iraq and Afghanistan, arguably the toughest problems we've confronted in decades, are nothing if not spectacularly complicated. Trying to size up these puzzles is like gaping at a home-made contraption that has mysteriously evolved into something that even its designers can no longer fathom, let alone operate and dismantle. Is there an owner's manual for this thing? Can it be unplugged? If we figure out where it's getting fuel, can we starve it and hope it expires?

"Look at the military PowerPoint slide of the Afghanistan war, a labyrinth of cross thatching lines and arrows swirling around words like 'insurgents' and 'coalition capacity' and 'priorities.' When we understand this slide, said Gen. Stanley A. McChrystal, who leads the American effort in Afghanistan, 'we'll have won the war.'

"At the same time, we're learning more about the financial instruments that caused our economic collapse, and it's now clear that 'exotic,' the adjective of choice, won't suffice. Synthetic collateralized debt obligations are impenetrable on purpose, built for maximum opacity. They're also lethal mysteries to companies like AIG, an insurance firm whose supposed expertise is assessing risk. AIG needed an $85 billion government loan to remain solvent.

"You sense that the march toward complexity has turned into a sprint in the debate about health care reform and even the gargantuan oil spill in the Gulf of Mexico, challenges so baroque, with so many disparate and moving parts, the best you do is hope that someone in charge understands them. Complexity used to signify progress – it was the frisson of a new gadget, the riddle of some advance in technology. Now complexity lurks behind the most expensive and intractable issues of our age. It's the pet that grew fangs and started eating the furniture…."

"Just about every profession has become more complicated in recent decades. The sheer volume of data and rules that must be grasped by a certified public accountant, for instance, has exploded.

"Says Gary Giroux, a professor of accountancy at Texas A.& M. The bible of the business is the portentously named *Original Pronouncements*, a book that at it heftiest a few years ago ran to roughly 10,000 pages.

"A century ago, Mr. Giroux says, there were no accounting courses, let alone, *Original Pronouncements* because accountants were just guys who double-checked the math of corporations to ensure that there wasn't internal fraud. What happened?

"'There was no income tax until 1913,' he says, 'and before the New Deal there was no Securities and Exchange Commission.'

"It's been fashionable for some time to bash accounting for its encyclopedic list of rules and standards, which is perhaps why a public relations rep at the Financial Accounting Standards Boards can come across as a little defensive when asked about the size of the group's most famous door-stopping tome. But you can't understand where all these regs came from without realizing that they made possible, and mirrored, the growth of the economy.

"Which gets us to the worrisome part of the complexity of problems we face today. Instead of improving our lives, it's vexing them."

But stop right there! The essence of our problem is not its complexity, but the rigged-up scam of trying to handle a complex problem with ever-increasing numbers of variables with a solution of just two independent variables – supply and demand. And the Lord knows with the numbers of PhDs around, they cannot have forgotten that first-year high school course in algebra enjoining us not to try solving equations with, say, 30 or 2,000 independent variables with solution of just two independent variables – "supply" and "demand."

From that the only conclusion to be drawn is simple enough, though it leaves society headed for destruction unless it is resolved. Those PhDs in Economics have been given the choice of early retirement or, never being hired, by universities unless they keep quiet about what they learned in the first-year high school course in algebra – you cannot solve a problem of more than two independent variables with less than that number of independent variables in your search for the solution.

So let us stick to the original problem, and bring back a knowledge of our history and of the work of the great economists, so we can equip ourselves to handle all the suppressed variables in economic problems beyond the only sacred two that are tolerated in the economics at most universities today.

Failing to do so, to save the privileged position of speculative, deregulated mega-banks, can only be a scam to limit society in this matter to simple two-variable solutions.

W.K.

day that number wasn't precise.

"In practice, the special purpose vehicle, or SPV, will be able to lend more than €440 billion, since it allows crisis-hit countries to pledge their bonds as collateral against further loans from the ECB.

"The ECB meanwhile began buying debt of weaker euro-zone countries in bond markets Monday a controversial role that put the ECB in the role of propping up wayward economies.

"Only on Thursday, ECB President Jean-Claude Trichet had rejected European banks' pleas for the central bank to buy euro-zone government debt, Global stock markets and the euro plunged. By Friday, ECB officials say markets had turned 'dysfunctional.'

"In a phone call with Ms. Merkel on Friday, US President Barack Obama called on Germany to act to stem the escalating crisis in global markets, say people familiar with the matter. US Treasury Secretary Timothy Geithner agitated for a more decisive euro-zone response in several conference calls with other Group of Seven finance ministers, these peoples said, and made specific critiques of European proposals."

A Forgone Outcome

Clearly with a former bank official now a high Washington bureaucrat, the chances of the repressed character of investment in human capital is not likely to be allowed to the fore.

"On Friday evening when euro-zone leaders gathered in Brussels to give their formal approval. To aid for Greece, Mr. Trichet spoke of a worsening pan-European crisis and called for swift action, EU officials said.

"As they sat down to dinner, the yield on Portugal's bonds rose to more than eight percentage points over what ultra-safe Germany pays to borrow for two years. EU officials realized that Portugal's trajectory put it just a few weeks behind Greece, which rapidly lost access to capital markets in April.

"Leaders agreed that something big was needed over the weekend to turn around market sentiment towards the euro zone, the official said. French President Nicolas Sarkozy, with support from most leaders present, pushed to announce a 'European stabilization mechanism' that Friday night, say people familiar with the matter. Ms. Merkel insisted governments take the weekend to weigh options and present a plan before markets opened Monday.

"Meanwhile, Mr. Trichet, with support from US Federal Reserve Chairman Ben Bernanke in Washington, said European governments needed to take more forceful action of their own before central banks would consider radical steps, according to people familiar with the talks.

"Mr. Sarkozy, who had for weeks agitated for bolder European action, pressed for the ECB to play a role, too. Ms. Merkel reported that the ECB was independent and couldn't take orders from national governments.

"No precise agreements was reached Friday.

"Mr. Sarkozy canceled a Saturday trip to Moscow, where he was due to attend a parade to mark the 65th anniversary of the end of World War Two. Ms. Merkel, fearing a German no-show would upset the Russians, flew to Moscow. She called other euro-zone leaders from there.

"Over the weekend, France and a majority of euro-zone members argued that the EU's executive arm, the European Commission, should borrow funds on capital markets and lend them to a stricken euro-zone nation, EU officials said.

"Berlin objected.

"Euro-zone finance ministers were set to meet at 3 pm Sunday in Brussels to broker a deal. German Finance Minister Wolfgang Schaeuble had barely arrived when he suffered a reaction to his medication and was taken to the hospital, EU officials said.

"Ms. Merkel dispatched her former chief of staff, German Interior Minister Thomas de Maziere on a Luftwaffe plane to stand in for the finance minister.

"Arriving around 8 pm, Mr. de Maziere took a tough stance against letting the EC run the bulk of the bailout funds, EU diplomats say.

"Other governments warned that markets were opening in Australia. Finally Germany and France settled on creating the SPV, allowing the package to be announced before Tokyo opened.

"The SPV reduced the burden of borrowing on indebted countries like Italy, while giving Germany control over aid disbursements. Several countries – including Italy – claimed credit for the breakthrough. The SPV 'must be a great idea because apparently, we all had it,' said a senior French official.

Now direct your mind back to McGeer's great discovery that the credit of modern governments need neither gold, silver, nor speculative mega-bankers to realize the vast credit arising from our government's investment in human capital.

W.K.

Once a Nation Suppresses Its History It Is on a Tossing Sea without a Compass

The Globe and Mail (14/05, "Leap in temporary foreign workers could create social unrest, critics say" by Joe Friesen) informs us: "Three years ago Canada passed a significant milestone when, for the first time, it accepted more temporary foreign workers than permanent residents.

"It marked a major shift in policy for a country that historically was built through permanent immigration, and one that could have long-term consequences for Canadian society. A new study from the Institute for Research on Public Policy suggests that the rapid growth of the temporary foreign worker program could undermine the model of integration that has so far made Canada's consensus on expanded immigration the exception among Western nations.

"Since 2002, the number of temporary foreign workers in Canada has nearly doubled. The program is in part a response to an aging population, but increasingly workers are sought for the unpalatable or poorly paid jobs Canadians simply refuse to take on.

"The study's co-author, University of Ottawa professor Delphine Nakache, says although the program may solve short-term labour shortages, it may also be short-sighted.

"'We were traditionally a country of permanent immigration,' Prof. Nakache said.

"'Now the landscape is changing. When people spend years in the country we can't expect them to leave once we don't need them any more.'

"The program's growth, from about 100,000 temporary foreign workers in 2002 to more than 250,000 in 2008, has created a kind of permanently temporary work force, Prof. Nakache said. The situation is somewhat reminiscent of European guest programs, which spawned years of social unrest in countries such as Germany, she said.

"'Being a temporary foreign worker gives you less legal status than a permanent resident,' she said. 'You can't benefit from training or language services. You cannot benefit from all settlement services…. If you're not happy at a job or in the hands of an abusive employer you may well find it harder to move jobs.'

"Immigration Minister Jason Kenney said comparisons to Germany are alarmist and have no relevance to the Canadian experience. 'Here's the truth. Those who want to shut down this program, essentially the labour unions and those in their employ, they have to tell the orchard farmer in the Okanagan that his business will go under because no one will help with the harvest,' Mr. Kenney said. 'The critics of this don't even try to balance their critique with the very real and urgent labour shortages that are being faced by many businesses. They disingenuously dodge this issue by suggesting the employees are being underpaid or exploited.'

"NDP immigration critic Olivia Chow described the increase in temporary foreign workers as a terrible policy that breaks with Canadian tradition. 'It's bad for the economy, because it depresses wages and is a disincentive to invest in potentially more expensive Canadian workers,' she said. 'Migrant workers have no capacity to put down roots in their community. Most can't bring their families and build neighbourhoods and communities. Because their status is precarious they're open to abuse.'"

Doors to Immigrants Closing in Our Globalized World

"New statistics released by Mr. Kenney's department Thursday show that the number of temporary foreign workers admitted in 2009 was 178,640, well below the number accepted the year before. He said the reply to complaints he receives from employers is that it has become more difficult to take advantage of the program since regulations, such as requiring the job to be advertised to all Canadians, were tightened during the recession.

"Although the program was initially created to help address the need for highly skilled workers, the majority of successful applicants now work in low-skilled jobs. Nearly half go to Alberta and BC, many of them to work as meat-packers, construction workers or care-givers. They can apply to become permanent resident either through the provincial nominee program, or in the case of more skilled workers through the Canadian experience class.

"The government has promised regulatory changes to limit temporary foreign workers to four years in Canada, but they have yet to be enacted, At the moment permits can be extended indefinitely."

Such a record bespeaks a wobbly hand on the rudder. It cuts us off from the shameful as well as the glorious chapters of our history. The shameful ones of course was our deportation of the survivors of the Chinese who had been imported to help build the most dangerous stretches of our railway system, with no small loss of life, only to be deported back to their homeland once the job was done. Their women folk were rarely allowed entry. And today the Chinese community in Canada is amongst the most highly educated sectors of our population, and an essential bridge with their homeland that has become the most dynamic player in the world economy.

Moreover, you cannot proclaim a globalized economy, and then qualify that world outlook merely to serve the needs of mega-financial gambles.

Our very technology – the relative ease of international travel has produced ever-tighter relationships between continents. For years the phenomenon of the so-called "snowbirds" who migrated annually between the farms in mountainous valleys of Italy to do much of the harvesting in the Argentine and back again.

That, however, was an oddity celebrated in poetry and prose. Today the world globalization is far more basic. What is lacking in the groping of governments is the suppressed notion of human investment as the best that a government can make. It is in fact prepaid and its "expenditure" is a reinvestment rather than a debt.

To tap the full significance of that revelation would require that we repossess our history and its lessons. We are then very much back to our starting point. We must reclaim our history wholly, fully, including our gropings and the invaluable lessons that emerged from that process.

William Krehm